

MAGADAN OBLAST REGIONAL PROFILE

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SUMMARY

Magadan Oblast is a steadily developing region that offers good economic prospects for both Russian and foreign investors. It is a leading gold producer in Russia. In addition to vast precious metals deposits, it also possesses unconfirmed oil and gas reserves offshore the Sea of Okhotsk. The region's investment promotion policy is aimed at attracting more potential investors and providing an improved business environment for joint ventures. The recently introduced Magadan Economic Area project provides its participants with tax and customs privileges and benefits. End Summary.

GENERAL INFORMATION

Magadan Oblast occupying 461,400 square kilometers in the so-called "Extreme North" area of Russia is the ninth largest territory in Russia and furthest from Moscow. It is also one of the most scarcely populated territories (225,600 people). Over half of the population (129,800 people) lives in the city of Magadan, the capital of the Oblast.



This northern territory is characterized by diverse and highly peculiar wildlife, which is due to different climatic conditions of taiga, forest-tundra, and tundra zones there; permafrost is ubiquitous throughout this area, and the southern and inland parts of it differ significantly in their climates. Forests are dominated by larch and mountain pine. The most valuable forests grow on the coasts of the Sea of Okhotsk and in the Kolyma River area. The coterminous northern part of the Sea of Okhotsk is rich in pollack, salmon, herring, cod, crab, shrimp, squid, seaweed, as well as pinnipeds (primarily seals).

Magadan Oblast has been widely known as a mineral storehouse. Its mineral riches include more than 11 percent of proven placer gold reserves, 15 percent of lode gold, and about 50 percent of proven silver reserves in Russia. The probable reserves of precious metals are 3-6 times greater than their proven reserves.

In addition to well-known gold and silver deposits, there are also payable prospects of copper, complex ores, molybdenum, tungsten, mercury, and antimony, various non-ferrous metals, and ornamental colored stone. Large lignite and coal deposits are also explored there. There are dozens of building material deposits including gypsum, volcanic ash, and facing stone.

The probable reserves of the Magadan offshore hydrocarbons come to more than six billion tons. About 25 types of hot springs, mainly chloride and sodium-calcium ones, are located throughout the territory of Magadan Oblast. The overall flux of the local hot springs totals about 24,000 cubic meters a day.

TRANSPORTATION INFRASTRUCTURE

Magadan Sea Port carries out nearly all the cargo transportations to the Oblast. The port disposes of all the necessary infrastructure and technical facilities to unload and run different cargo operations.

Magadan city has an international airport providing passenger and cargo transportation with the other territories of Russia, NIS, and foreign countries. The Airport serves all types of passenger carriers, as well as heavy cargo planes.

Kolyma highway connects Magadan Oblast with the other regions of Russia. The total length of roads is 1,700 miles. Motor transport prevails in the system of internal transport.

The Magadan branch of the Far Eastern Telecommunication Company is the main provider of telecommunication services in Magadan Oblast. The regional telecommunication network integrates and maintains different automatic telephone systems, toll lines, cellular radiotelephone, facsimile and paging links.

INDUSTRY

Magadan Oblast's leading industry sectors include mining (60 percent of the overall production volume), power industry (20 percent), and food processing. Transportation and communication sectors, as well as fishing and fish processing, are also well developed.

Mining

Gold mining dominates the region's industrial production. Precious metals mining and production account for the primary share of the Oblast's budget. The industry is also the primary employer and income provider for the local population. The increase of gold production during 2003 was largely attributed to the introduction of new ore units of Kubaka, Shkolnoye and Juliet as well as administration's efforts for promotion of the stream deposits development. The other gold ore and gold-silver deposits that are currently being developed include Agatovskoye, Vetrenskoye, Dukat, Lunnoye, Natalka, Nyavlenga, Svetloye. *Kolyma Gold Refinery Plant* has been steadily increasing its industrial output of chemically pure precious metals produced from ore and placer deposits occurring not only in Magadan Oblast but also in Kamchatskaya Oblast, Sakha (Yakutiya) Republic and Chukotsky Autonomous Region.



During 2004, 23.967 tons of gold were produced in the Oblast, which is a 3.109 ton decrease from 2003 results.

Silver runs second after gold in commercial significance to Magadan Oblast. Silver is a co-occurring metal in all the gold ore deposits in addition to the independent silver deposits. In 2003, Magadan Oblast ran first in silver production in Russia. During 2004, the silver mining volume was 645.907 tons (up 14.322 tons). The increased production was possible due to two companies: Serebro Magadana JSC and Serebro Territorii JSC, which are engaged in the development of Dukat and Lunnoye deposits in Omsukchanskiy District.

Mining Volume of Selected Minerals during the First Quarter of 2005

	1st quarter of 2004	1 st quarter of 2005	Growth rates (%)
Gold, kilograms	3,641.0	3,677.3	+ 1.0
Silver, tons	224.0	220.2	- 1.7
Coal, thousand tons	233.7	255.2	+ 9.2

Oil and Gas

The estimated recoverable reserves of the North-Okhotsk shelf bordering the Magadan Oblast coastal territory amount to 1.4–2.5 billion tons of oil and 2.7-4.5 trillion cubic meters of gas condensate. At this time, an open international competition is being organized for the right to explore and develop oil production in the shelf. The development of the *Lora* copper-molybdenum ore deposit is yet another promising project. The estimated reserves are 850 million tons of ore, 4 million tons of copper, 200,000 tons of molybdenum, and 11.8 thousand tons of silver.



Processing Sectors

During January-April 2005, Magadan Oblast processing operations produced \$94 million worth of goods.

Performance of Selected Processing Operations during January-April 2005

	January-April 2005 USD thousand	% to January-April 2004
Processing industry total	43.919.298	+12.8
Production of food stuffs, including drinks	31.642.105	+23.5
Textiles and clothing manufacture	59.649	7.2 times
Wood processing and production	94.737	5.1 times
Publishing and printing	547.368	+10.3
Chemical industry	126.316	2.5 times
Production of non-metal mineral products	1.554.386	2.4 times
Metallurgy	5.312.281	-39.2
Machine building and equipment manufacture	2.459.649	+21.6
Electronics and optics production	185.965	2.4 times
Production of transportation vehicles and equipment	263.158	+56.3
Other production	828.070	-22.3

Food Processing

Food processing industry is reported among the primary sectors of the Magadan Oblast economy. Its share in the gross regional production varies from 11 to 16 percent. The sector performance is highly dependent on the overall operation of the fishing sector. Its share in the food industry reaches 78 percent.

Fishing and Fish Processing

Fishing industry is traditionally ranked second in importance for the Oblast economy after the mining sector. It is also the only exporting industry. As of April 2005, 31 enterprises were engaged in fishing activities. The primary fishing areas include North-Okhotsk, West-Kamchatskaya and Kamchatsko-Kurilskaya zones of the Okhotsk Sea. Some 38 types of fish and sea products are currently allowed for commercial fishing, 15 of them constitute 82 percent of overall production in the sector. During the first four months of 2005, production of

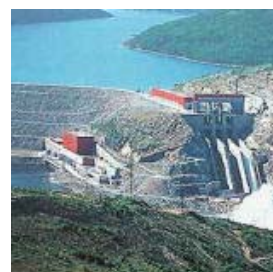
fish and sea products totaled 29,685 tons, which was a 26 percent increase to the corresponding period of 2004. Pollack and herring accounted for the primary volume of quota. The share of Pollack is 23.4 percent, 14,468 tons were caught in the first quarter of 2005 (grew 21 percent). The share of herring is 36.3 percent, the catch volume during January-April 2005 totaled 14,223 tons (grew 31 percent). Shrimp accounts for 1.6 percent of the available quota, crab – 4.7 percent.

The largest and most profitable fishing operations of the Magadan Oblast not only develop their own quota but contract with other fishing operations of the Oblast and RFE. These enterprises possess their own fishing fleets. They include:

- Tikhookeanskaya Fishing Industry Company Ltd (7,715 tons)
- Magadanriba Ltd (7,341 tons, including 5,714 tons of own quota)
- Tralcom JSC (4,654 tons)
- Omakhtonskiy Shelf Ltd. (3,089 tons, including 1,633 tons of own quota)
- Marine Ltd. (1,999 tons, including 1,301 tons of own quota)
- Seamar Ltd. (1,964 tons, including 304 tons of own quota)

Power

The primary power engineering enterprises in the Oblast are Magadanenergo JSC and Kolimaenergo JSC. Kolyma Hydro Power Station located at the Kolyma River is the main power generating station in the region, providing the lowest energy costs in the Russian Far East territory. During 2004, production of electric power grew 3.2 percent compared to 2003 and totaled 2,510.0 million kwt per hour. Production of heat was 3,002 thousand GKal, the same as in 2003.



Small Business

As of January 1, 2005, 2,031 small enterprises were registered in Magadanskaya Oblast, or 19 percent of the total number of businesses (2 percent increase compared to 2003). Small businesses employ 14 percent of the population. The largest number of those employed by small businesses were in industry – 48 percent, trade and catering – 18 percent, construction – 16 percent.

Small businesses plan to increase their share in the regional production. In 2004 they produced \$223 million worth of goods and services, accounting for 34 percent of gross production.

Consumer Market

During the first quarter of 2005, retail trade turnover grew 4.7 percent and totaled \$73.5 million. The retail trade turnover per capita grew 16 percent and totaled \$420. The retail trade turnover during January-April 2005 was comprised of trading organizations and individual entrepreneurs (80 percent); the share of markets was 12 percent.

Income

During January-March 2005, the population income increased 10 percent and totaled \$156 million. Income exceeded expenditures by \$9.3 million. Population spent 54.3 percent of its income on consumer goods and services, 10.5 percent on taxes and payments, 24.3 percent – savings, 4.9 percent – on purchase of foreign currency. The real available income during the first quarter of 2005 fell 1 percent.

Income per capita during January-March 2005 totaled nearly \$300 (\$342 in March 2005). The minimum living wage in the first quarter of 2005 totaled \$152 and grew 8 percent compared to the 4th quarter of 2004. The average nominal wage of employed population was \$435 (up 14.3 percent).

FOREIGN TRADE & INVESTMENTS

In 2004, the foreign trade turnover of Magadan Oblast grew 58.7 percent and reached \$161.4 million. The export and import sectors both increased. The export share amounted to 44.7 percent of the region's overall foreign trade turnover; the import share totaled accordingly 55.3 percent. There remained the raw material focus of the export structure: fish and sea products constituted 70.2 percent, metals and metal wares – 16.6 percent, machinery, equipment and vehicles – 12.8 percent.

The U.S. share in the trade turnover of Magadan Oblast totaled 32–42 percent, Japan – 20-22 percent, the Republic of Korea – 12-16 percent, Canada – 5-6.5 percent. Cyprus, China, Italy, Germany and Singapore were the other partners.

2004, Export structure, % Magadan Oblast	
Foodstuffs	70.2
Metals & metal wares	16.6
Machinery, equipment & vehicles	12.8
Miscellaneous	0.4

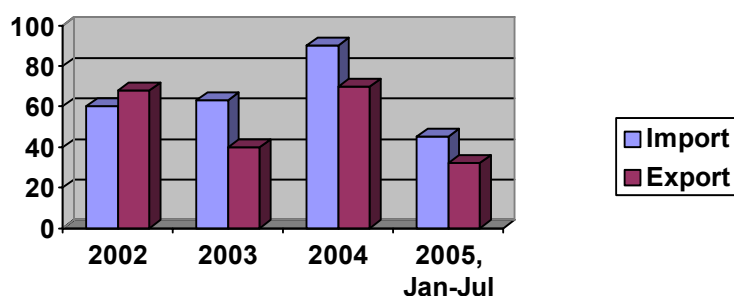


In 2004, the export share in fish and seafood catches increased 10 percent. The share of processed sea products such as crab preserves and fish flour totaled only 1 percent of the export volume. About 90 percent of sales took place outside the Russian customs border. Japan, the Republic of Korea, the United States, Great Britain, and China were the main buyers. Machinery, equipment and vehicles, chemical products, fuel, metals and metal wares, and foodstuffs prevailed in the import structure. The volume of machinery, equipment and transport vehicles had been increasing since the 2002; in 2004, its share totaled 56.5 percent.

The share of services in the foreign economic activity decreased during the period. In 2004, the export of services fell 6 percent (\$2,240.1 thousand), import – 20 percent (\$9,572.3 thousand).

Magadan Oblast believes that incoming tourism is a key future prospect for increased foreign activity in the region. During the past three years, tourism-based income increased three times. The number of foreign tourists visiting the region grew 6.5 times. Magadan Oblast provides various “exotic” entertainments, for example, hunting tours, rafting on mountain streams, mountain skiing, mountaineering, and “gold” tours.

Foreign trade turnover, USD mln, Magadan Oblast



In 2003, capital investments in the regional economy (mainly in industries) totaled 3.3 billion rubles, or \$118 million. Non-ferrous metallurgy, fish industry, deposit exploration and mining were among the most active sectors. During the first six months of 2004, the foreign investment inflows into the economy amounted to \$28.5 million that is 3.8 times greater than in 2003. The prime investors were the U.S., Canada, Germany and Great Britain.

Foreign investments in Magadan Oblast during January-March 2005 (thousand USD)

	Cumulative as of January 1, 2005	Obtained during January-March 2005	% to January-March 2004
Total	89,810.0	1,175.9	79.0
- direct	48255.8	41.9	-
-- input in capital stock	44,068.8	41.9	-
-- loans from foreign co-owners	3,536.2	-	-
-- other direct investments	650.8	-	-
- other investment	41554.2	1134.0	76.0
- - other credit	41549.2	1134.0	76.0
- - other	5.0	-	-

United States accounted for 96 percent of the overall investment during the period, New Zealand – 4 percent.

MAGADAN ECONOMIC AREA PROJECT

Aiming to create favorable economic conditions in the region, the Federal Duma passed *the Magadan Economic Area* national law, which came into effect in 1999. In the same year, the Magadan Economic Area (MEA) was established providing its participants with tax and duty privileges, and exemption from paying federal budget taxes. The import goods are brought into the area under duty free conditions and without any economic sanctions. Goods manufactured in the MEA and exported throughout Russia and abroad are not subject to customs duties and any other levies except the export charges at the Customs.

From 1999 until December 31, 2005, the MEA participants are exempt from paying the federal budget taxes except charges to be paid to the Pension Fund and the Social Insurance Fund of Russia.

Since January 1, 2006, till December 31, 2014, the MEA participants are exempt from paying the profits tax for it is invested in the socio-economic development of Magadan Oblast.

The MEA participants use revenues resulting from their tax and duty exemption for their business expansion and new industries development thereby promoting investment activity in the Oblast.

The revenues yielded under the MEA project since 1999 and re-invested in the local economy are as follows: tax exemptions - \$82.14 million, customs duty exemptions - \$57.2 million. Moreover, about \$75 million has been transferred to the Fund for Socio-Economic Development of Magadan Oblast, 27 percent of which are invested in the regional economy.

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